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Family Values: Influencers in the Development of Financial and Non-financial Dynamics in Family Firms

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Abstract

The role of family values is considered here as one potential contributor to heterogeneity. The pursuit of profit as an end goal may be key for many family businesses but there are well-documented cases of businesses where corporate citizenship and philanthropy are integral to the business model. Earlier work has highlighted that where one family has a predominant level of control in a business, their family values may assume greater importance and thereby be more likely to influence strategy. Within this chapter, we propose that the concentration of family values that occurs when one family has a predominant level of control within the business may be a key contributor to the development of financial and non-financial dynamics, representing one way in which strategy is developed and implemented.

Keywords: Family business, financial decision-making, family dynamics SME, household decision-making

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Introduction

Family values are a sometimes contentious topic, even within families themselves, and diverse views are often linked to concepts of tradition and behavioural expectations. In this chapter we have chosen to pull together the opinions and contextualise them as being defined here as principles or standards of behaviour (Oxford English Dictionary, 2016). Where the family run a business, family values take on much clearer dimensions and indeed have developed into an area of some considerable study, focussed around the manner in which the values of the family influence business behaviour. Indeed, a recent report by PWC (2017) highlighted the common perception that the two defining, and distinguishing, characteristics of a family business are stewardship and heritage, often associated with a sense of duty towards the business. By managing the business assets and heritage, it is argued, values that may underpin business sustainability are distributed inter-generationally.

In parallel with this, family businesses are important, forming a cornerstone of economies in most developed countries and contributing socially and economically across countries, continents and geo-political divides in terms of innovation, job creation and economic cohesion (Poutziouris et al, 2006; Kets de Vries, 2007 pxiii, IFB 2008, Seaman et al, 2015; 2016). This consensus has been achieved despite the acknowledged lack of clear definitional clarity around family business; indeed Sharma et al (1997) and Chua et al (1999) identified 34 operating definitions of a family business in the extant literature (Getz et al, 2004) and there is little reason to suppose that this number has diminished Sharma, 2004; Collins and O'Regan, 2011). Different authors within the definitional debate do, however, share some common concepts and themes. Most agree that a business is an organisation that is profit making *at least in intent* (Alcorn, 1982; Getz et al, 2004; Seaman et al, 2016). Similarly, most agree that in a family business one family has a predominant level of ownership and may also work within the business (Getz et al, 2004; Seaman et al, 2016) and that the presence of the family within the business influences that business to a greater or lesser extent (Seaman and Bent, 2017). Whilst a related debate has developed around levels of family engagement (Astrachan, 2004) and extended to include concepts as familieness and familiarity, this chapter focusses less on the definitional debates and takes as a starting point the conclusion by Phan and Butler (2008) that where one family has a predominant level of control within a business, the values of that family contribute to common understandings of acceptable behaviour and integrity within the business. It is important to note here that there is no assumption within the literature or indeed this chapter that the family values will always exert a positive influence; rather, the precept here is that close family members are likely to share some common values and that where they run a business the presence of shared values may influence the decision making process. Whether that influence represents a positive or negative influence on, for example, business integrity is a separate question that this chapter does not seek to address and indeed empirical research in this area is sparse. Whilst further empirical research would be valuable, the methodological challenges involved in overcoming self-reporting bias in the description of personal values and indeed the links between self-reported goals and needs (Schwartz et al, 1997) are likely to extend to self-reporting of family values and complicate potential research in this field.

Finally, we bring together within this chapter a third and substantive area of academic study that considers how financial decisions are made. Financial decision making by individuals and indeed groups has been frequently examined through the orthodoxy of standard financial models constrained by assumptions of rationality. Although the reality of family behaviour is difficult to square off with theoretical models, the financial requirements of Family Businesses (like any other small or medium sized firm) requires them to adapt to the expectations of Financial Services Institutions.

This chapter contributes to the discussion on how the decision-making process of small family businesses differs from that of financial institutions. This is of growing importance since small family businesses tend to have limited access to banks and short-term sources of funding and are particularly vulnerable to solvency risks. The research proposes a conceptual framework to allow for further development of risk assessment models to help financial institutions to make decisions on credit and services to small family businesses.

Family, Family Values, Financial and Non-Financial Dynamics

Definitions of family vary and the historical context is an important area that presents some challenges for researchers. Social historians, anthropologists and psychologists have described a wide variety of forms and norms for that entity described as 'family', over a wide variety of historical time periods and social settings (Doherty and Boss, 1991; Bloch and Harrari, 1996 Seaman and Bent, 2017). Indeed, the word family is derived from the Latin 'familia, meaning 'household servants, family' and closely linked to famulus (servant). In more recent times, there is some evidence that the word 'family' was used to mean a group of slaves (Coontz, 1993), but more recent commentary has reached general agreement that a family is:

‘ a group of individuals linked by blood, living arrangements, marriage or civil partnership who consider themselves to be family, who often choose to spend time together and may live together.’

Adapted from: Family: Business Dictionary (2016)

While the historical perspective is interesting, there are also a variety of different contexts where the word family is used in the 21st century, including the familial analogy in business (Seaman et al, 2014) and indeed varying social structures in countries where religion or tribal affiliation form a core societal unit. This definitional debate is critical, however, because it provides a backdrop to the understanding that family norms and values can only be fairly considered in the context of the time and place in which they are formulated (Bloch and Harrari, 1996¬) and lends weight to on-going discussion in the family business literature about the importance of context in family (Seaman and Bent, 2017). Family values, in turn, are defined here as:

‘the principles and standards of behaviour, one’s judgement of what is important in life’

Oxford English Dictionary, 2016

The importance of family firms and the impact of family values on decision making are important in a general sense. This chapter focusses on financial decision making as it relates to family dynamics and considers the complexity of the small firm context.

The case of Financial Decision-Making in Family Businesses

'Standard' Financial Decision-Making

There are an almost infinite number of financial decisions made every day by governments, firms, households, and individuals[1]. In the UK when it comes to individuals and households, most of these decisions are concerned with the consumption of goods and services to satisfy basic needs, the payments of bills and invoices, but occasionally major investments that require financing or selling major assets (ONS, 2017). Governments and firms on the other hand focus on working capital, managing financial risks, long-term investments, profitability and sustainability, and maintaining a healthy balance sheet amongst others, all of which require the use the techniques and processes generally accepted by all participants in financial markets (Brennan & Solomon, 2008). Family businesses, in particular those that are under management and control of their founders, by definition will be more likely to be constantly straddling both household and business considerations when making financial decisions (Haynes, Walker , Rowe, & Hong, 1999).

The issue is of course that these financial decisions are not made following the same rationale, methodologies, techniques, or even considering the same type of assumptions and/or variables (Koropp, Grichnik, & Kellermans, 2013) (Steijvers & Voordeckers, 2009). For the purpose of simplicity the discussion could be limited to two types of economic actors: firms and households. From an institutional perspective (the financial intermediaries and institutions whose ultimately set the price of assets and liabilities in financial markets), firms are assumed to be economic actors who behave rationally: this means that all their decisions can potentially be modelled within the

[1] According to the Bank for International Settlements in the reporting countries alone there were approximately 374,780 million payment transactions by non-banks in 2015. Bank for International Settlements, CPMI-Red Book Statistical update, December 2016, pp. 445-547

confines of a theoretical framework that permits evaluating future risks and forecasting net returns to investment (Barton & Gordon, 1987) (Modigliani & Miller, 1963).

The 'rationality' of this type of firms is embedded in financial models through a framework of economic theory and determined by standardised assumptions on behaviour (Blume & Easley, 2008). These models enable financial institutions to make assessments of the decisions made by firms against the expected behaviour implied by the assumptions or, in some cases, offer alternatives or expand on the assumptions if needed. The outcome of financial decisions is difficult to predict as the markets for goods and services are changing constantly along the conditions under which they operate. Therefore, in order to forecast the financial impact of management decisions, the development of models requires limiting the number of variables through assumptions about behaviour (Bauer & Hammerschmidt, 2005) (Thomas, 2000). This reductionist approach allows participants to simplify the appraisal of potential financial impact and make long-term commitments that are essential to economic growth and stability by basing decisions upon expected rather than observed assumptions on behavior.

Insert Figure 1 about here

In financial markets the relationship between the assumptions used in decision models and the expectation of market participants is symbiotic: if an economic actor behaves in a manner inconsistent with the expected assumptions the markets will react in such a way that the impact of the unforeseen behaviours are eliminated (Berg & Lein, 2005). For example if a firm's management decides to grow by acquiring more debt and this is perceived by the market as 'too risky', then all lenders will increase their cost of funds to the firm and 'communicate' to the market the risk level associated with the firm. If the management of a publicly traded firm makes business decisions that are incompatible with the market's assessment of the firm's value, the price of its share (and therefore its overall value) will be checked through market operations (buying and selling of shares) in organised exchanges.

In order to be able to operate efficiently, governments and firms need to manage their funds as efficiently as possible and this requires constant access to financial markets in order to borrow and invest short- and long-term funds (Allen & Santomero, 1998). This means they need to stay integrated and follow the rules, that is, behave 'rationally' within the parameters of generally accepted models, whether it is pricing, valuation, or risk assessment. They are idiosyncratically 'rational': their strategies and operations are all designed to work within the confines of an accepted standard economic model (Arrow, 1989). This approach is universally accepted and has allowed firms and financial institutions to interact within an agreed framework of concepts and techniques leading to common expectations and understanding about markets, without which the exchange of goods, services and financial assets would be too onerous and costly (Cabantous & Gond, 2011). Firms that operate within the parameters of rational models will therefore follow a series of steps to inform a decision and in turn serves as justification for the funds provider.

Insert Figure 2 about here

In contrast, even after the financial crisis of 2007-2009, small and medium-sized firms (SMEs) do not have the scale to participate directly in financial markets and need to do so through intermediaries: banks, investment firms, insurance companies, pension and other funds, and sometimes government agencies (de la Torre, Martinez Peria, & Schmukler, 2010). Their financial needs are relatively small and too infrequent to justify the costly infrastructure required to have a direct presence in financial markets, but the intermediaries will evaluate their prospects as they are assessed themselves. As the financial behaviour of SMEs is not shaped by the markets' expectations (like the intermediaries assessing them) when assessed through traditional models they will be find to have a greater deal of complexity and unpredictability (Ekanem, 2010). This is of course only a problem when small or medium-sized firms need funding or other financial products: their risk will be assessed against a model based on a market-reinforced behavioural assumption and everything else will be ignored, including the full spectrum of influences driving their financial expectations (Pederzoli, Thoma, & Torricelli, 2012), but the conditions under which SMEs operate are clearly different from those of larger firms.

Insert Figure 3 about here

These behavioural assumptions are critical because they will determine whether a small or medium-sized firm will be able to access funds from financial markets. They are, like traditional financial decision-making models, derived from the Standard Economic Model or SEM. The key assumption of the SEM is the requirement for individuals and firms to be rational decision-makers (Blaug, 1978) (Stigler, 1987). This means that individuals and firms are driven by an individual motive: to maximise utility (individuals) and profit (firms) and are not assumed to consider the impact of their decisions on others. It is also assumed that individuals and firms have access to all the relevant information, the ability to understand and manipulate it, and the prescience to adjust the risk assessment about situations whenever there is new data that may affect their prospects (Bayesian probability operators). The assumptions also include consistency in terms of preferences: if an outcome A is always preferred over an outcome B, and this one in turn is preferred over C, then A will also be better than C. If market participants align their behaviour and expectations to these assumptions, the market itself becomes 'rational' and therefore the models are a closer reflection of reality (Jehle & Reny, 2010).

However useful and accepted these models have been as prescriptive and predictive tools, their underlying assumptions are not a true reflection of how the 'real' world behaves (Kahneman & Tversky, 1979). A simplified view of economic agents and their interactions require that the way in which they assess risks, their preferences and choices are limited to a manageable number of options, preferably one. This is not necessarily a 'bad' thing to institutional decision-makers who can accept these provisos and manage expectations on model outcomes since they have the necessary expertise and capabilities in data analysis, and deal with others with the same understanding of the requirements, strengths and weaknesses of the models. Firms with dedicated departments dealing with the complexities of working capital management, long-term funding, investments and risk exposure benefit from this common knowledge that allows them to replicate (however imperfectly) the behaviours in the assumption of financial models.

The use of decision-making models based on SEM assumptions become rather problematic for smaller firms that do not operate in such an environment and do not have the necessary resources or capabilities to make an ‘objective’ analysis of the variables of a financial problem are making the decisions. These small firm owners will only come in contact with major financial institutions when applying for loans for capital investment or when being assessed as potential suppliers by major corporations. Without the pressure of other market participants, regulatory requirements, and separate planning and control systems it is difficult for family businesses (and any other small firm) to behave as the rational decision-makers assumed by financial models. Studies on family businesses have found alternative goals that are usually not considered by traditional financial analysis, including but not limited to social and personal long-term achievements (Astrachan & Zellweger, 2008).

In their day-to-day operations family businesses will not be expected to have access to complete information with regards to the markets for their products and services, the human capital necessary to analyse risk within a timely and cost effective manner, or a consistent set of strategies for the purchase and management of productive assets. During the process of start-up of when in need of external sources of finance the need may rise to operate within the realms of rational models, but in daily operations as owner-managers the majority of decisions they will make are similar to those of households and include money management, daily expenditures, surplus funds, asset maintenance and short-term contingency planning. These are the type of decisions that do not require extensive planning, agreement of intermediaries nor meet the minimum requirements calculated through financial models. Family businesses are not expected to make decisions frequently in an environment where financial assets and liabilities are exchanged in high volumes for amounts that require them to adjust their behaviour to fit the demands of a model.

Financial decision-making in small businesses

The financial decisions made by small businesses may be simpler than those of corporations but not with less risk to the firm, and can be broadly classified in terms of their magnitude and frequency (although some are driven by social or cultural needs). With regards to magnitude and frequency, financial decisions in small businesses (and medium-sized businesses to that effect), tend to fall within three types: cash expenditures in relatively amounts of money (usually not more than one hundred) on a frequent basis (daily), scheduled payments of weekly, bi-weekly, monthly or quarterly current obligations made from the current account and with values in the hundreds or low thousands, and occasional high-value purchases (investments in major assets) . The latter are very infrequent and happen during start-up or expansion phases and usually require financing from a financial institution, therefore family business owner-operators need to follow a standard set of established procedures in order to assess the decision (business plan with financial projections) in order to obtain the funds. The decision-making process is less orthodox when it comes to both daily spending and scheduled payment of obligations, as they are clearly not made according to the assumptions of the standard economic model, highlighting that autonomous decisions of habitual and exceptional items will be dependent on the availability of funds only. Power relations will determine the levels of negotiation required in case there is more than one decision-maker.

Insert Figure 4 about here

The small and frequent transactions (habitual and exceptional purchases) are particularly outside of the scope of the SEM behavioural assumptions since these do not require business owners to have full information on alternatives, the impact of the expenditure on their financial objectives, and to make adjustments to their spending patterns depending on changes in external circumstances. Instead, this type of decision tends to be made through an instinctive almost primal process that follows cognitive scripts (defined here as semi-automatic decisions made routinely) formed through time by the influence of social forces and cultural experiences. The automaticity of these decisions means that these choices are made with little consultation amongst the owner-managed firm even when its members have equal participation in the control of the business' affairs.

A characteristic of small businesses that clearly does not adapt to the framework of institutional financial decision-making models based on the SEM is the assumption of egoistic or individual utility or profit maximisation. Small businesses must account for actions that may have an impact on 'kin obligations' (employing family members), social standing in the community, long-term human capital goals (children's education), and/or cultural obligations (events, charitable contributions, etc.). These types of expenditures not only affect the income statement and cash flows of the firm but also divert economic resources from immediate investments (a preoccupation of SEM frameworks). These non-economic decisions have a financial impact as their desired outcome may represent some sort of future financial or social remuneration, however this is beyond the realm of traditional financial models. In general, these decisions within small businesses tend to be made with a 'collective mind' and based on a common appraisal of desired economic, social, and cultural outcomes that will have an impact on the owner-manager.

Dispute resolution

The influence of the Standard Economic Model extends beyond the investment and funding decisions of firms that operate within the parameters financial markets. Corporate governance and dispute resolution also tend to be confined within its space since any action considered using an alternative methodology or data may be challenged using the generally accepted model. The market will pass judgment on those decisions and in many cases the risk it will give to unusual transactions will become a foregone conclusion, as economic actors will behave as if the perception was real. Shareholders and Boards will also judge the effectiveness of management according to these rules, so the model will become arbiter of their actions, as this is the standard by which they assess their ability. Notably, also, in SMEs the process of conflict resolution goes beyond the presentation of alternative sets of data analysis. Decision-makers will need to resolve differences in their values and priorities, both personal and business related, as well as their expectations of how the decision will affect the benefits or influence in the firm's management. These negotiations are in the middle of two forces: power relations and the desire for harmony. If agreement is reached and the decision is made there is a second phase of reflection with regards to the outcome and its impact on the dynamics of the relationship.

Insert Figure 5 about here

In small firms there is of course the possibility of differing opinions and conflict on the best course of action, but rather than using a standard model to resolve conflict any disagreement tends to be related to individual hierarchies of values, subjective assessments of risk and return, and/or the personal aspirations and benefits of each decision-maker. The goals of financial decisions in small businesses tend to be subject to some level of collective agreement however, these are usually influenced by dominance and the dynamics mutual interactions, in particular when ownership is split and the different parties (partners, spouses, family members) attempt to impose on the others their perceptions of the overall gains (economic, social or cultural) and risks of any decision. This also applies to reaching agreement amongst members with differing financial capabilities and assigned (or assumed) roles within the firm who may have a different understanding of the potential risks and returns of financial decisions.

Daily expenditure and financial decision-making in households

The power dynamics in autonomous decisions of importance and instinctual spending on minor purchases is a characteristic that is found in household financial decision-making. Studies on the decision-making process are useful in building an understanding of family business dynamics as they can also be classified in terms of their magnitude and frequency, and as in the case of small firms, for the most part their 'heads' tend to make frequent (daily) and relatively small amount cash decisions determined by their need to satisfy basic needs (food, transportation, health and well-being, etc.), entertainment and social interactions (presents, invitations, etc.), and following culturally prescribed or expected behaviours (charity, contributions, tips, etc.).

As in the previous discussion, their decision-making process is very different from the orthodox normative models that describe a sequence of logical steps under assumptions of rationality. Like small firms, households do not have access (nor seek) all relevant information or have the capability to evaluate and select the best alternative based on pre-determined economic objectives. On the contrary, households tend to make decisions as the need arises: not in any logical sequence but concurrently and as they appear, without assigning time or resources in proportion to its complexity. Financial decisions in households are not insulated and analysed separately from daily events, and this is probably a key element in understanding its similarities to that of Family Businesses. The key question is whether the latter tend to make their decisions more like households than firms, in which case decision-making models with a behavioural finance set of variables and assumptions would be more suitable.

In order to attempt an answer to this question it is necessary to identify some of the characteristics of household decision-making by looking and adapting some of the models used to understand their economic behaviour. A conceptual model developed by Kirchler (1989) is a useful starting point as this was used to analyse the structural characteristics of the household in terms of dominance and mutual interactions. The interactions amongst the main decision-makers in the household can be classified within a scale that ranges from altruism to self-interest, with the former leading to 'harmonious' relationships. Financial decisions made when the interactions are driven by altruistic motives tend to result in more optimal outcomes (not necessarily in a financial sense but in terms of their objectives) because the key members of the household will share the information and methods used to analyse it, be equally accountable for the outcome, share responsibility in terms of the effort or resources needed, and make a common effort in order to implement the decision taken.

When the interactions within the household are less 'harmonious' financial decision-makers will approach their choices with a greater degree of self-interest. The process of making decisions and all interactions have elements of 'credit' (an expectation of a similar response in the future), 'barter' (a 'like-for-like' transaction), and of courser 'selfishness', when the objective is to maximise one of the decision-makers' wants or needs. This is when power and dominance come into play: as the relationship moves down the scale from altruism to egoism, the household member who has the greatest influence will be able to manipulate the decision-making process to his/her advantage. The greater the power differences within the household, the more decisions will be limited to views informed by a single set of information, analysis and objectives. Importantly, too, the nature of the household's relationship will determine whether decisions are made autonomously or in cooperation. When there are unresolved issues in terms of power, values, and/or goals, decisions will be pulled towards the 'egoism' end of the spectrum and although they could require a cooperative approach they will be made autonomously by only a single dominant member or sub-group within the household.

Insert Figure 6 about here

As discussed previously in terms of small firms, the financial decisions made by households include disbursements such as cash distribution (allowances), periodic daily spending, as well as allocating money for savings as well as regular payments such as bills and insurance to protect existing assets. In terms of frequency and magnitude, the number of decisions a household makes about cash 'outflows' tend to be substantially larger than those with regards to 'inflows' as the latter relate to income generating activities that are significant but largely infrequent. Frequent transactions tend to be of relative low magnitude in relation to the household's income and are usually made almost automatically without much of a decision-making process involved. These financial transactions include paying for services used on a daily basis (public transport, tolls, etc.), purchasing inexpensive products of familiar brands with known quality (newspaper, coffee, etc.) and other type of payments that have become part of a regular routine.

Also as in the case of family businesses, frequent and repetitive decisions do not require any type of evaluation and analysis since their individual impact on the household budget seems insignificant, and they tend not to be thought of in the aggregate. This type of decisions will not be open to discussion with other household members unless at any point they call for a commitment of a significant part of the household's income. As the magnitude of the disbursement increases there will be a greater requirement for consensus amongst household decision-makers: in addition to its impact on the cash availability there may be social or cultural repercussions for all household members. The same holds for cash inflows, as changes in employment or income generating assets my have an impact on the household's economic security.

This is when disagreement may rise given both the power and nature of the interactions and depending on the differences amongst household decision-makers there may be various types of conflicts. One of these can be the product of fundamental differences in the goals of the partners. There can be also problems related to the assessments of the information, method, and options involved in the decision-making process. These arise when the household agrees on the value and the importance of an alternative but arrive at different preferences because they have either received different information or evaluated it in different ways. Finally there may be conflicts related to the distribution of profits and/or costs related to a decision. In this case there may be a general agreement on the purpose and the type of decision being made, but not on how to distribute the costs or benefits of the decision.

At this point of the discussion we bring together household and small firm financial behaviour. These seem to be mostly in terms of frequent decisions that although may not seem to have a major impact on the firm's income, on aggregate they may have serious effects on their cash flow management. This type of decision-making process has been studied through the lens of Behavioural Finance and offers an insight to how individuals either in the context of a Family Business or Household makes financial decisions.

A conceptual model of family business decision-making

The proposed conceptual model is based on the idea that financial decision-making in family businesses will be influenced by rational decision-making models (based on the Standard Economic Model) for significant investments, and a heuristic based approach characteristic of frequent purchases in small businesses and households with influences such as power struggles, emotions and relationships. Those decisions that are frequent and of relatively low magnitude tend to be mainly 'non-rational' and their analysis can be carried out within the framework of behavioural economics. This field has identified cognitive processes such as heuristics and biases that provide information processing and analysis shortcuts to quickly provide 'acceptable' answers to financial problems. In the aggregate this simplification process tends to result in systematic errors in high frequency and low magnitude transactions, which in the case of Family Businesses are related to working capital management. The reason why this is important is because all these small and frequent transactions are related to cash flow management and liquidity and solvency problems are main culprit of small business failure. The various factors that differentiate how family businesses approach financial decision-making will have greater influence in the process in smaller firms that do not depend heavily on financial institutions (banks, exchanges, etc.) for loans or investment channels. Although these 'non-rational' forces may influence traditional corporations, these may have a bearing in other aspects of decision-making.

Insert Figure 7 about here

The heuristics analysed in behavioural finance research are simple and efficient rules that have been learned through socialisation or become part of evolutionary processes and behaviours. Research has identified many heuristics and biases in the process of financial decision-making, in particular the formulation of judgments about the risk to the outcome of a decision, and also finding solutions to complex tasks when there is not enough time or resources to find answers. These heuristics and biases are developed individually and communally, through experience and knowledge or acquired through socialisation and evolution, so they work well under most circumstances. However, these automated systems may be used for the wrong task and this can lead to systematic errors or cognitive biases.

It is important to note that the decision-maker is aware that he/she is using a short cut to find a quick solution to a complex problem. The risk of making a mistake through a loss in accuracy is sometimes outweighed by savings finding the appropriate data and securing the necessary capabilities and resources to analyse it (Payne et al, 1993, Shah & Oppenheimer 2008). The heuristics and biases research carried by Daniel Kahneman, Amos Tversky, and others has generated two main results that are worth considering when trying to understand how family businesses make financial decisions under risk: a list of biases, fallacies, or errors in probabilistic reasoning, and explanations of these biases in terms of cognitive heuristics. Kahneman and Tversky reasoned that when making predictions and judgments under uncertainty, people do not appear to follow probabilistic calculations or predictive statistics, and instead, they rely on a limited number of heuristics that sometimes yield reasonable judgments and sometimes lead to severe and systematic errors. The presence of an error of judgment was demonstrated in experimental settings by comparing people's responses to questionnaires either with established facts or with an accepted rule of arithmetic, logic, or statistics.

The distinctions identified by Kahneman and Tversky with regards to judgments under uncertainty have been further analysed by social and evolutionary psychologists. Kahneman and Tversky originally identified three general-purpose heuristics: availability, representativeness and anchoring and adjustment. This opens the question of how these main heuristics and biases could potentially influence the decision-making process of family businesses. A conceptual model for carrying out this research would look as follows:

Modelling the Impact of Family Values on Business

At the risk of stating the obvious, family businesses tend to have family members in key positions of ownership, leadership or management. This chapter takes the view that the inclusion of a number of different individuals from one family tends to lead to a concentration of values from that family, which may in turn influence decision making. We also acknowledge here that the term 'family values' does not represent one value set, nor are family values always positive Rather, we argue very simply that where a number of key figures within a business share a degree of family background and history, a concentration of similar values is likely, albeit with the proviso that one or more strong leaders may be in a position of considerable influence. Similarly, while family values are one core influencer of decision making there are many others including the views of advisors, non-executive Board members, investors, current markets and indeed family members who may not be directly involved with the business but who still exert some influence over the 'value pool'. History may also play a role and the importance of formalised governance structures as a mediating factor on decision making should not be underestimated, but the role of family values in decision making represents an area where further research would be appropriate. The model presented in the figure below represents an initial and literature-based attempt to consider the spectrum of businesses within the term 'family business' and to encapsulate the factors that may influence financial decision-making. This conceptual model provides the key variables for further research on the factors and variables that drive financial decision-making in family businesses.

Insert Figure 8 about here

Key to an understanding of the model presented in Figure 8 is an understanding that the space on the spectrum occupied by a firm will vary according to the size, stage of development and ambitions for the firm. By modeling the influencing factors explicitly, however, we create a basis for future and empirical research that allows the stage of development of family firms to be encapsulated as the basis for discussion within the context of consultancy or education.

Discussion

The influence of family values on business decision-making is not easy to define or measure as values are shaped by social and cultural expectations as well as personal traits and attitudes towards relationships and entrepreneurship. The idea of this chapter was to start the discussion on the foundations for a theoretical framework of analysis, informed by psychology and behavioural finance, with which to isolate specific value-based observable behaviour and relate it to the impact of family decision-making.

In essence we started from the hypothesis that a family-run business (in particular small or medium-sized owner-managed) will have different priorities and ultimate goals than those of a non-family business, and this will have an impact on how they approach their financial decisions. The discussion was confined to the financial dimension because (1) the impact of the decisions is measureable (to an extent) and (2) there has been ample research in terms of behavioural variables in financial decision-making (albeit in the realm of trading in equities and other types of financial products).

In the first part of the analysis we focused on how 'traditional' financial decision-making takes place in businesses that interact with financial institutions and markets. We highlighted how firms follow prescribed models with generally accepted assumptions that help estimate predictable outcomes and risk (therefore allowing for external investors to make assessments of risk and return and price appropriately). Businesses that need funding (start-up, investment in growth, etc.) or any type of financial product will at some point be required to use these models (either directly through business plans or indirectly through loan and mortgage applications). As there are secondary markets for most of these financial products, valuation models based on commonly accepted assumptions, data, and procedures make these transactions more efficient and widen participation. To a certain extent the same applies to the day-to-day running of their cash and working capital management operations that can be evaluated by market participants and permit a risk assessment of the firms' performance.

The discussion then moved into how financial decisions are made in small businesses. These tend to be simpler than those of market-influenced firms but not with less risk, and we broadly classified them in terms of their magnitude and frequency. We argued that most financial decisions in small businesses tend to be related to cash expenditures in relatively small amounts of money (usually not more than one hundred) and a frequent basis (daily). Owner-managers agree to scheduled payments of weekly, bi-weekly, monthly or quarterly current obligations made from the current account with values in the hundreds or low thousands, but these are hardly ever revised. The decision-making process is less orthodox when it comes to both daily spending and scheduled payment of obligations, as they are not made according to the assumptions of the standard economic model. Instead, this type of decision tends to be made through an instinctive almost primal process that follows cognitive scripts (defined here as semi-automatic decisions made routinely) formed through time by the influence of social forces and cultural experiences. The automaticity of these decisions means that these choices are made with little consultation amongst the owner-managed firm even when its members have equal participation in the control of the business' affairs, and this may lead to conflict.

In small firms conflict related to financial decision-making is not resolved using governance rules (based on standard models) because disagreements are related to individual hierarchies of values, subjective assessments of risk and return, and/or the personal aspirations and benefits of each decision-maker. Although the goals small business financial decisions tend to be subject to some level of agreement, there is usually the imposition of some type of dominance in interactions, in particular when ownership is split and the different parties attempt to influence others with their perceptions of the overall gains (economic, social or cultural) and risks of any decision. This also applies to reaching agreement amongst members with differing financial capabilities and assigned (or assumed) roles within the firm who may have a different understanding of the potential risks and returns of financial decisions.

We move in our discussion into the realm of family matters and how decisions are made within a scale between altruism and egoism. We argue that the nature of the household's relationship will determine whether decisions are made autonomously or in cooperation. When there are unresolved issues in terms of power, values, and/or goals, decisions will be pulled towards the 'egoism' end of the spectrum and although they could require a cooperative approach they will be made autonomously by only a single dominant member or sub-group within the household. There may also be fundamental differences in the goals of the partners related to the assessments of the information, method, and options involved in the decision-making process. These arise when the household agrees on the value and the importance of an alternative but arrive at different preferences because they have either received different information or evaluated it in different ways. Finally there may be conflicts related to the distribution of profits and/or costs related to a decision. In this case there may be a general agreement on the purpose and the type of decision being made, but not on how to distribute the costs or benefits of the decision.

Finally we built a conceptual model (based on a behavioral finance framework) taking the view that the inclusion of a number of different individuals from one family tends to lead to a concentration of values from that family, which may in turn influence decision making because of the potential conflict inherent in decision-making. The idea is that 'family values' does not represent one value set, nor are family values always positive We argued very simply that where a number of key figures within a business share a degree of family background and history, a concentration of similar values is likely, albeit with the proviso that one or more strong leaders may be in a position of considerable influence. Similarly, while family values are one core influencer of decision making there are many others including the views of advisors, non-executive Board members, investors, current markets and indeed family members who may not be directly involved with the business but who still exert some influence over the 'value pool'. The role of family values in decision-making represents an area where further research would be appropriate

Future Research Directions

Research in family businesses would greatly benefit from a deeper understanding of the financial decision-making process. The cultural, social, and behavioral factors unique to family-run businesses and the relationship with finance needs to be understood in more detail.

Implications for Practice

Financial decisions will determine the viability of firms in particular their relationship with funds providers. Financial institutions need to have an understanding of how these firms differ from mainstream businesses and how to meet their financial requirements.

Conclusions

Underpinning this chapter lies one, relatively simple premise: the financial dynamic within family business differs from the dynamic observed in traditional, corporate-model businesses. This circumstance exists, in part, because of the different power dynamics that exist between both individual and institution and indeed between different members of the family. In setting out some of the factors that influence financial decision making in family business, this chapter seeks to provide the basis for future and empirical research However, it is acknowledged that a myriad factors influence financial decision making and some – such as culture and/or religion – would merit more detailed consideration.

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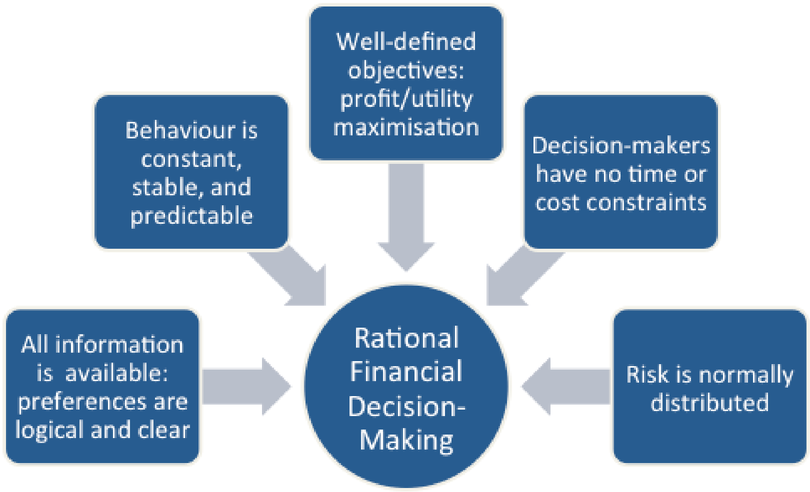

Figure 1: Rational decision-making assumptions.

Figure 2: Financial decision-making cycle.

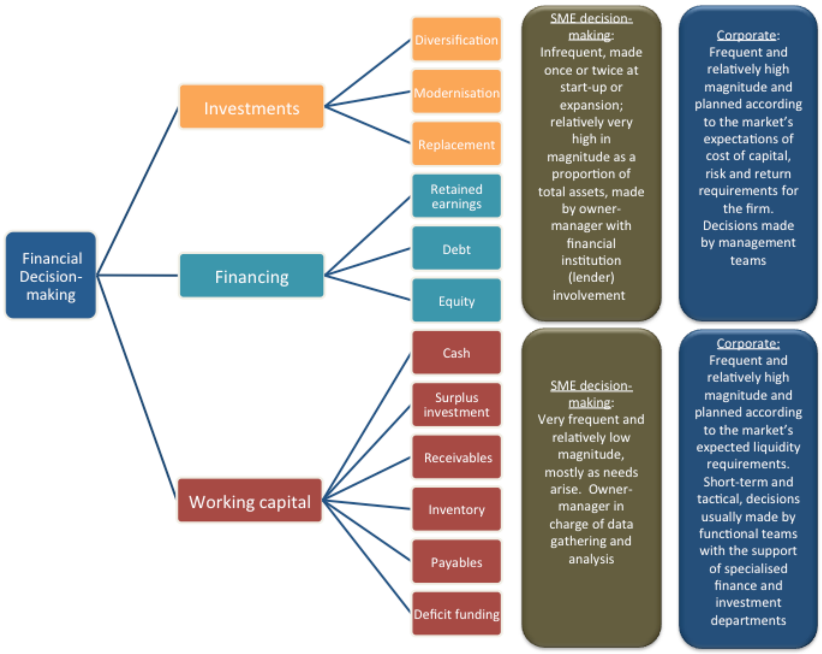

Figure 3: Corporate Vs. SME rational financial decision-making.

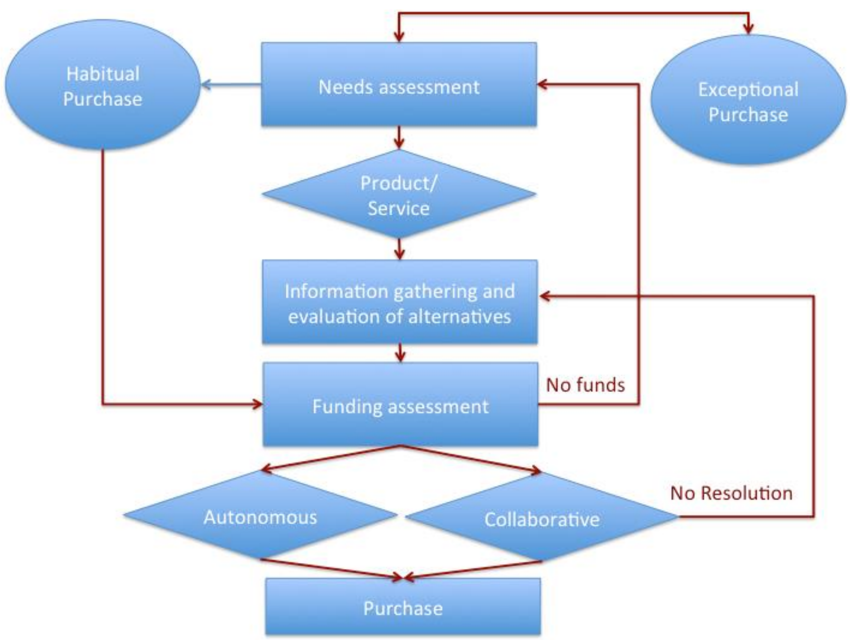

Figure 4 SME Financial decision-making process.

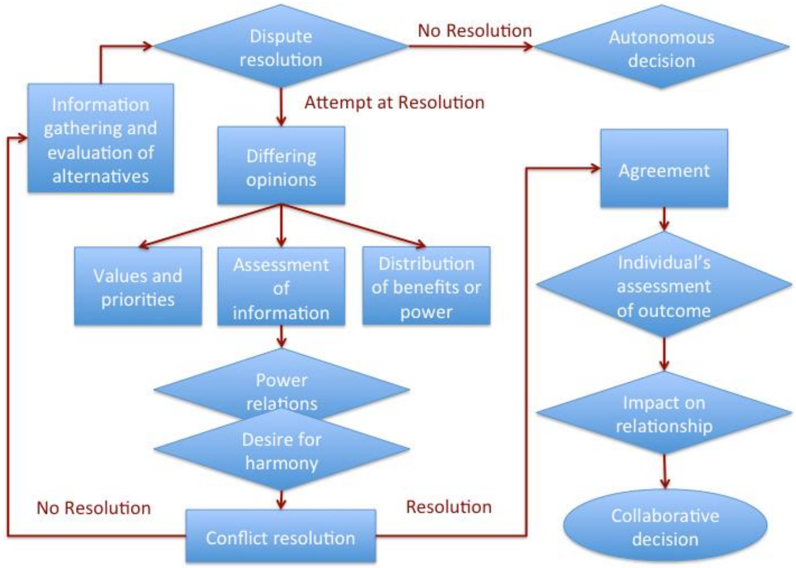

Figure 5 SME Decision making conflict resolution.

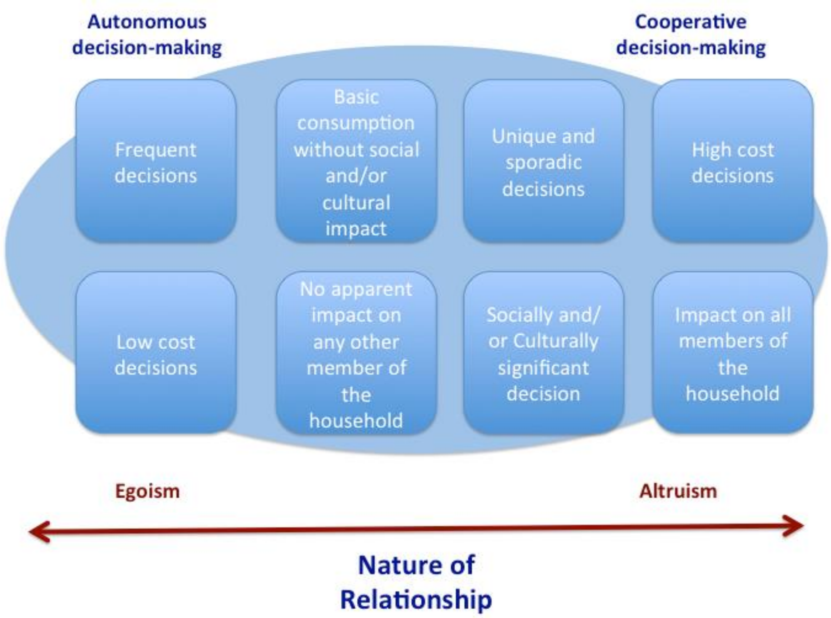

Figure 6: Household decision-making.

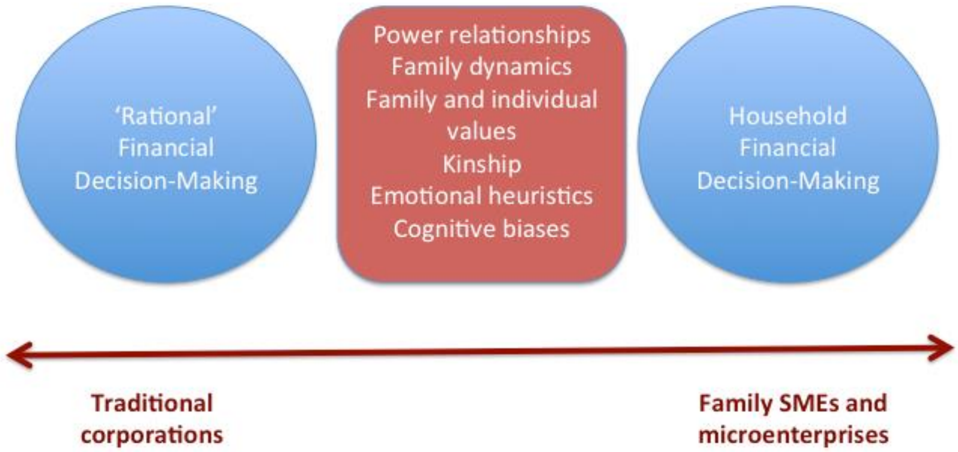

Figure 7: Family business decision-making model.

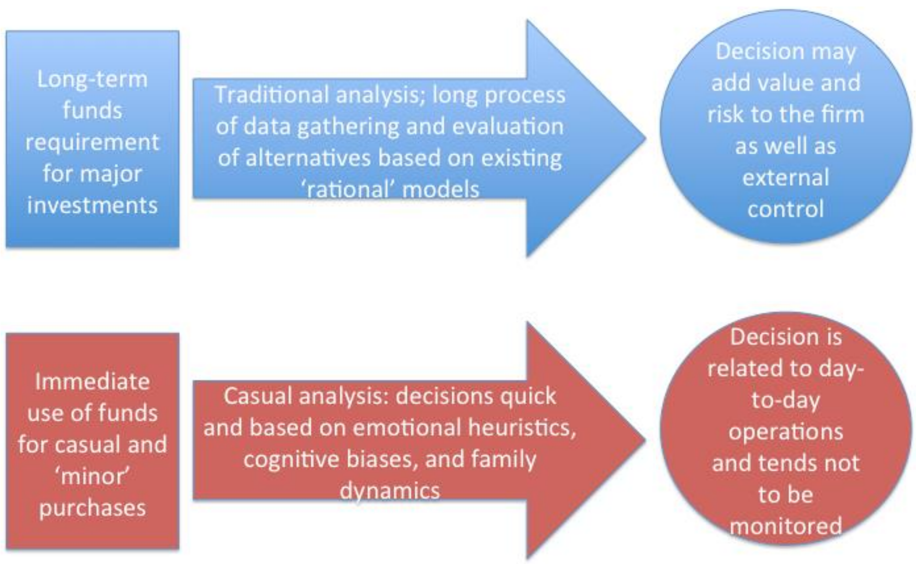

Figure 8: Family business decision-making model.